

The Daily Press: □ A defense spending crisis in January? Think summer

by Hugh Lessig, June 24, 2012

Automatic cuts in U.S. defense spending will take effect in January 2013 if Congress does nothing about it. That's what it says on paper.

In reality, the drag on the defense industry is already in the works, portending serious consequences for Hampton Roads and Virginia into the summer and fall, analysts and elected officials say.

A recent survey of smaller businesses engaged in ship construction, maintenance, repair and supply found that many are already contemplating layoffs and cutbacks. The prospect of an 11th-hour deal around Christmas would provide little comfort to companies that must make key decisions in the coming weeks.

Building a ship takes years, and so does the planning.

"If you need 20 tons of steel, you don't pick up the phone and it's delivered the next day," said Ashley Godwin, a senior defense adviser for the Shipbuilders Council of America. "It requires purchases well in advance."

The burden falls heavier on small- and medium-sized businesses that don't have the financial flexibility or lengthy project lists of larger corporations, she said.

"The smaller companies, a lot of them go hand to mouth, month to month," she said. "The don't have the cash reserves and they have small work forces."

The fallout from defense cuts will spread throughout the economy, said Barry DuVal, the former Newport News mayor and current president and CEO of the Virginia Chamber of Commerce. He's talked to smaller companies whose employees are in limbo, not sure what will happen.

"These people are not out buying automobiles or purchasing new houses," he said. "They're probably less interested in a vacation this summer. This sort of uncertainty creates a cloud on the economy, especially for states that are depending on defense spending."

Big word, big impact

The current crisis is rooted in the Budget Control Act that President Barack Obama signed into law last year. It created a bipartisan committee to find an additional \$1.2 trillion in savings over the next decade to reduce the budget deficit. The committee failed, so the law spells out mandatory, automatic cuts in defense and non-defense spending: \$600 billion each over the next 10 years.

That process is known as sequestration. If that's too much of a mouthful, consider the term used by Defense Secretary Leon Panetta before a Senate panel last week. The automatic cuts, he said, are a "meat ax approach."

But so far in this bitterly contested presidential election year, Congress has failed to strike a deal to avoid the cuts.

Republicans have refused to consider tax increases while Democrats are concerned about cutting entitlement programs. This week, the top Republican on the House Armed Services Committee released a video that painted the defense-cut fallout in stark terms and accused Democrats of blocking a solution.

Rep. Howard "Buck" McKeon took aim at Obama and Senate Majority Leader Harry Reid, and said Republicans have put responsible plans on the table. At the same time, he said, Democrats have offered no plan of their own.

The spot invoked the GOP's favorite son, Ronald Reagan, who advocated peace through strength, and interspersed archival black-and-white footage of ticker-tape parades, saying those who deserved a hero's welcome will instead receive pink slips.

"The time for guarded language," McKeon said, "has passed."

Fair enough, says Rep. Robert C. "Bobby" Scott, D-Newport News.

He agrees that sequestration would have a devastating impact on the military and defense industry. But he bristles at the GOP's insistence at extending the Bush-era tax cuts that are set to expire.

\$1 trillion

If Congress allowed the tax cut to expire on incomes over \$250,000, it would generate nearly enough money — \$1 trillion — to avoid sequestration, not only the cuts to defense, but the cuts to entitlement programs as well, Scott said.

Eliminating all the Bush-era tax cuts would generate \$4 trillion in savings over 10 years.

Republicans want to keep the tax cuts in place, as do some Senate Democrats. But to Scott, it makes no sense to extend the cuts, reducing the flow of money to the treasury, then figure out how to deal with the \$1.2 trillion in additional cuts through sequestration that no one wants to see.

"They are trusting the media not to notice that they are supporting a \$4 trillion tax-cut extension," he said, "hoping that nobody notices while we suffer through and commiserate how hard it is to find a trillion dollars for the sequester."

He said Republicans who rail against the size of government ought to spell out the

consequences of that policy.

"Is the water too clean? Is the air too clean that we don't need to regulate air pollution? Should we cut back on consumer regulation?" He asked. "The thing that frustrates me is that everybody gets to say 'we need to reduce the size of government,' and reporters write it down as if they said something."

Scott said no proposal for deficit reduction is popular. But given the furor over sequestration, he says the least unpopular choice would be allowing the tax cuts to expire on portions of income over \$250,000, then plowing that money into public works programs to create jobs.

That idea faces tough sledding with Republicans, who say taking money out of people's wallets is the last thing needed in this fragile economy. Democratic Sen Jim Webb of Virginia has a third course. He doesn't want to raise taxes on ordinary income. Rather, Congress should look at capital gains and dividends, where the most wealthy people make their money, according to a report this week in The Hill.

1 million lost jobs

The National Association of Manufacturers released a study Thursday that paints a stark picture if the cuts go into effect. It used a multiplier model that factors how layoffs affect the rest of the economy – what DuVal was talking about when he referred to workers not buying cars and homes.

By that yardstick, the cuts would cost more than 1 million private-sector jobs by 2014, including 130,000 manufacturing jobs. The unemployment rate would increase by 0.7 percent. The hardest-hit states would be, in order, California, Virginia and Texas.

If the situation does not change, Virginia will lose nearly 115,000 jobs in 2014 alone, the study says. The industries hardest hit by sequestration also spell bad news for the Old Dominion.

Aerospace, ships and boats and search/navigation equipment businesses top the list.

"We have aerospace in Northern Virginia and Hampton Roads, and we have ships and boats in Hampton Roads," said DuVal. "And the support of those is search and navigation. The gross number of jobs lost would have a devastating impact at a fragile time."